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BEFORE THE

Federal Communications Commission

WASHINGTON, D. C.

In the Matter of Review of the Commission's Regulations and Policies Affecting Investment in the Broadcast Industry	MM Docket No. 92-51

COMMENTS

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of America

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SUMMARY

Prudential fully supports the Commission's efforts to review and revise its Attribution Rules in order to remove unnecessary impediments and disincentives to funding of media industries. In addition to the amendments specifically proposed in the Notice, there are several measures available to the Commission which should be adopted to foster the stated goals. Specifically, Prudential urges the Commission to amend its rules to:

- Increase the voting stock threshold for attribution from 10% to 20% for "passive investors."
- Limit the attribution of interests for directors to only those directors sitting on boards of licensee corporations or corporations controlling licensees.
- For all limited partnerships (whether or not widely-held), apply equity ownership standards to non-insulated limited partnership interests, and clarify the insulation criteria.
- Clarify and relax the cross-interest policy to exclude interests held by passive investors.

Adoption of these changes and clarifications will aid substantially in facilitating media enterprises' access to capital.

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COMMENTS

The Prudential Insurance Company of America, by its attorneys, hereby files its comments in the above-captioned proceeding.[1] Prudential fully supports the Commission's efforts to review and revise its Attribution Rules[2] in order to

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1 Notice of Proposed Rulemaking and Notice of Inquiry in MM Docket No. 92-51, -FCC Rcd.- (rel. Apr. 1, 1992) (hereinafter "Notice").

2 Attribution of Ownership Interests, 97 F.C.C.2d 997 (1984), recons. 58 R.R.2d 604 (1985), further recons. 1 FCC Rcd. 802 (1986).

remove unnecessary impediments and disincentives to funding of media industries. As discussed below, Prudential believes that, in addition to the amendments specifically proposed in the Notice, there are several measures available to the Commission which should be adopted to foster the stated goals. Specifically, Prudential urges the Commission to amend its rules to:

- Increase the voting stock threshold for attribution from 10% to 20% for "passive investors."
- Limit the attribution of interests for directors to only those directors sitting on boards of licensee corporations or corporations controlling licensees.
- For all limited partnerships (whether or not widely-held), apply equity ownership standards to non-insulated limited partnership interests, and clarify the insulation criteria.
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Adoption of these changes and clarifications will aid substantially in facilitating media enterprises' access to capital.

I. The Current Regulatory Arrangements Impair Media Companies' Access to Capital Without Serving the Commission's Ownership Policies.

Prudential's experience in media investments provides a helpful illustration of the ways in which the current regulatory scheme impedes Commission objectives. As a mutual insurance company managing over 270 billion dollars in assets,

Prudential has provided substantial funds to the broadcasting industry. Through both equity investments as well as debt financing, Prudential has invested well over $1 billion dollars in broadcast, cable television and other media properties. A significant portion of these funds has been invested in minority-controlled enterprises in furtherance of the Commission's policies.

In the course of making its media investments, Prudential has incurred substantial costs in order to ensure compliance with the Commission's regulatory policies. These costs occur both at the time of the initial investment decision and throughout the life of the investment. Of particular importance in today's economic environment, some of these investments are in the process of being restructured in order to permit the companies adequate opportunity to adjust to the economic downturns which have burdened the broadcast industry in recent years. Regulatory costs occur here as well: The Commission's rules have significantly affected, and at times impeded, these restructurings.

Prudential has made its media investments for the sole purpose of achieving a satisfactory return for its owner/policyholders. Prudential is not, and never has been, interested in running a media company. Reflecting these objectives, Prudential's equity investments frequently take the form of non-voting stock (or options), or dependent upon the tax implications, insulated limited partnership interests.

Voting stock interests are typically limited to minority positions, with control residing in third parties. Debt financing, which often accompanies equity positions in the borrower, contains traditional lender protection provisions without influence over or interference with the daily operations of the borrowing company. This investment strategy is consistent with, but largely independent of, FCC attribution and ownership policies. Indeed, as the FCC rules recognize, there would be significant ramifications as a matter of insurance law were Prudential to attempt to involve itself in the management of these companies. The rules thus appropriately categorize insurance companies as "passive investors" and apply a higher threshold for cognizable voting interests held by such companies. The Commission's proposal to raise this threshold to 20% is consistent with this treatment and is fully supported by marketplace realities, as discussed below. While Prudential supports this aspect of the proposal, other remaining aspects of the Commission's attribution policies serve to undermine significantly the benefits of a certain, and higher, threshold.

II. Numerous Changes to the Rules Will Appropriately Serve the Commission's Objectives.

The Commission's review of its attribution rules is appropriately motivated out of concern for broadcasters' access to capital. In recent years, both macroeconomic conditions as well as difficulties facing broadcasters specifically have served to diminish the ready access to capital the industry had

historically enjoyed.[3] As the Commission has recognized, many of the microeconomic pressures leading to this dilemma are unlikely to abate. See generally, F. Setzer and J. Levy, "Broadcast Television in a Multichannel Marketplace," Federal Communications Commission, Office of Plans and Policy Working Paper Series No. 26 (June 1991). While the FCC's ability to ameliorate these conditions is necessarily limited,[4] there are measures available to the agency which can serve to improve the current circumstances. Most significantly, modifications to the current regulatory arrangements in order to create greater certainty to potential investors are crucial to the Commission's stated objective of facilitating access to capital. Under current conditions, the application of the attribution rules (and the cross-interest policy) remains sufficiently vague that potential investors may be deterred from opportunities on this basis alone. When coupled with the not insignificant costs necessitated by ensuring compliance, the rules pose formidable obstacles without serving any counterbalancing policies of the Communications Act. This

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3 Whereas unregulated industries facing analogous conditions have turned increasingly to foreign investors for their capital requirements, this avenue is largely foreclosed to broadcasters by operation of Section 310(b) of the Communications Act.

4 Of course, to the extent the economic uncertainties derive from the advent of technological progress and innovation resulting in new competition to broadcast and cable companies, the Commission has appropriately disclaimed any inclination to handicap marketplace outcomes.

proceeding thus offers the opportunity for the Commission to remedy at least some of the difficulties facing media industries without any sacrifice to other fundamental FCC policies.

A. The Voting Stock Thresholds Should be Increased as Proposed in the Notice.

Prudential fully supports the Commission's proposal to increase the voting stock thresholds from 5% and 10% to 10% and 20% respectively. In the case of insurance companies (or other "passive investors") such as Prudential, voting stock interests at 20% levels are qualitatively the same as 10%.[5]

Prior assumptions that a 20% block of stock would be sufficient to exert influence over management have been largely based upon the model of a publicly traded company. See, e.g., Attribution Order, 97 FCC 2d at 1006-08, 1013. Thus, as stated, the perceived problem is that "merely voting or trading large blocks of stock can affect the management of a company . . . even if [such effects are] inadvertent and unintended." Id. at 1013 (footnotes omitted). But this statement is far too

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5 This is especially so when an insurance company (or other "passive investor") holds this amount of stock but another shareholder holds a larger position. In such instances, the effect of the larger shareholder(s) is analogous to the Commission's "single majority shareholder" exception. Thus, at a minimum, the threshold should be relaxed to 20% whenever any other person or entity holds a larger block, regardless of whether this block exceeds 50%. Like the single majority shareholder exception, supermajority provisions which give minority shareholders substantial influence over the operations of the media properties would render the interest attributable.

broad; its logic would capture numerous other interests and rights which, in theory, "can affect the management" but are reasonably viewed by the rules as non-attributable. For example, the trading of large blocks of preferred stock has a similar potential to affect management, but has consistently and appropriately been treated by the Commission as non-attributable. See, e.g., Evening Star Broadcasting Co., 68 FCC 2d 129 (1978). Similarly, debt instruments may contain additional potential opportunities to influence management, but the mere potential has never resulted in debt being subject to the attribution rules. Indeed, debt instruments are not even examined by the cross-interest policy. Although any set percentage established by the Commission will be inherently arbitrary, there is little justification for not relaxing the low 10% threshold.

This is especially true in the specific context of passive investors. The investment motives of an insurance company simply cannot be presumed to transmogrify from that of a "passive" investor at a 10% level to an influential participant at 20%. The continuation of the requirement that a licensee certify that such investors have not exercised or attempted to exert influence over its affairs serves as a backstop to ensure that the underlying goals of diversity and competition are served.

B. The Attribution of Interests to Directors Should Be Limited.

Under the current attribution policy, any director of a FCC-licensed corporation is deemed to have a cognizable interest in the licensee. Similarly, a situation in which a director on the board of a media company serves as the representative of another entity will result in two cognizable interests: one held by the director individually and second by the entity which is represented by the director. These rules are rationally based upon the underlying policies they were crafted to implement: board participation in a licensee, or a corporation controlling a licensee, may often signal a degree of involvement in the media operations sufficient to implicate either the competitive or diversity concerns of the cross-ownership and multiple ownership policies. See Section 73.3555 Note 2(h). However, the literal reach of the notes goes much further by attributing cognizable interests not only to companies holding sufficient equity positions in media companies, but also to the directors of those investing companies. Thus, if Corporation A holds 11% of the voting stock of Licensee Corporation, all of the directors of Corporation A, as well as the directors of any boards controlling Corporation A, are deemed to have attributable interests in Licensee. The unintended consequences of the overbreadth of the notes are to impose substantial costs upon companies such as Prudential such that each and every member of its twenty-three member board must concern himself or herself

with running afoul of FCC rules notwithstanding the most peripheral involvement in media. Even where, as a technical matter, the notes do not pose an issue for Prudential but only for its directors (where, for example, the director serves on a media company board in his own right and not as a Prudential representative),[6] the costs ultimately fall upon the company to ensure compliance by its entire board. The direct costs of compliance for the investment community, e.g., internal monitoring, should not be underestimated by the Commission. More importantly, there are substantial indirect costs. These include both a diminished ability on the part of investors to attract highly qualified directors with specific media experience, and similarly, an inhibition on the part of the financial community to share their expertise by serving on the boards of media companies.[7] Perhaps most troublesome are the rule's chilling effects upon investor incentives to invest the media properties.

Moreover, the Commission's "certification" exemption is inadequate to reduce the burdens of rule. The larger costs

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6 See WKBW-TV, Inc., 19 FCC 337, 339 (1954).

7 The application of these notes takes on a special irony in the case of certain of Prudential's directors. Under its New Jersey State charter as a mutual insurance company, approximately one-fourth of Prudential's board are "public directors" and thus appointed by the New Jersey Supreme Court. Plainly, such directors do not serve on multiple boards (or otherwise hold multiple attributable interests) in order to affect the local media operations of companies in which Prudential may have chosen to invest.

reside in monitoring these positions to even know in the first instance whether "certification" must be made. More importantly, Prudential and other similar institutions should not be required to forego the expertise of its board members in managing investments. Director participation in such instances involves financial decisions as to whether to make or maintain investments, and thus poses virtually no risk to the Commission's diversity and competitive ownership policies.

For these reasons, Prudential respectfully urges the Commission to clarify, and to the extent necessary, modify the notes as currently written to attribute interests to directors (and, where appropriate, back to the entities they represent) only where the board on which the director sits controls, directly or indirectly, the licensee/media company.[8] Otherwise, the Commission's rules attribute interests far too removed to be of any genuine interest or concern to the underlying ownership policies.

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8 Thus, if Company A holds an attributable, but non-controlling interest in Licensee B, the directors of Company A would not have an attributable interest in Licensee B and would be able to hold attributable interests in other media properties in the same location without running afoul of the FCC's ownership rules.

C. Equity Ownership Standards and Amended Insulation Criteria Should Be Adopted for Limited Partnership Interests Regardless of the Size of the Partnership.

The Notice proposes to amend the insulation criteria for limited partnership interests so as to permit some degree of participation by limited partners in the removal of general partners without creating attributable interests or losing the benefits of the "multiplier" for purposes of assessing compliance with Section 310(b), 47 U.S.C. § 310(b). In response to petitions filed with specific reference to business development companies, the Notice proposes to amend the criteria for all "widely-held" limited partnerships. Additionally, the Notice proposes to create a threshold limit, presumably analogous to the 20% limit proposed for voting stock, under which even non-insulated limited partners would be deemed to have non-cognizable interests.

Unfortunately, these proposals -- like the rules they would amend -- reflect a fairly fundamental misconception of the limited partnership investment vehicle. At least in the case of institutional investors like Prudential, the choice of capital formation -- corporate or partnership -- is driven largely by tax considerations. By no means are such decisions made by reference to the degree of participation or influence to be acquired. Either model can be molded to reflect a desired locus and level of control or influence. Indeed, many "debt" instruments used today may not depart significantly in economic effects from traditional equity vehicles. As stated

earlier, whatever form its investment may take, Prudential has independent and substantial imperatives to refrain from participating in the operation or management of these companies. This fact is recognized in the attribution rules governing voting stock held by "passive" investors; it is wholly ignored under existing requirements if the investment occurs via a limited partnership.

Prudential fully supports the Notice's proposal to amend the rules to apply an equity ownership standard to non-insulated limited partnership interests. More specifically, the Commission should allow non-insulated limited partners to hold equity interests below the 20% threshold without attribution, regardless of the size of the partnership. Prior rationales for treating limited partnerships distinct from corporations for purposes of measuring the degree of influence or participation do not reflect commercial or legal realities. In Prudential's experience, and as generally reflected under state partnership law, there is no material difference in the participation and/or voting power of a 20% limited partnership interest and a 20% voting stock interest. Moreover, such observations hold whether or not the partnership interests or the stock is widely or closely held.

Additionally, the insulation criteria should be clarified. In response to the petitions filed by Equitable Capital Management Corporation and Kagan Media Partners, the Notice proposes, inter alia, to allow insulated limited

partners in certain limited partnerships to vote on the removal of the general partner at will. Notice at ¶ 16. In the past, the Commission has observed that such powers, at least under certain conditions, could result in a limited partner having substantial control or influence over the general partner via the threat of removal. For this reason, the FCC has previously required that the right to remove general partners be qualified. It is self-evident that application of a 10/20% threshold would substantially remedy this concern while simultaneously removing one impediment to media investment. In addition, however, Prudential urges the Commission to clarify the insulation criteria in this regard. The insulation guidelines are vague as to what types of limited removal power are permissible to remain insulated. See Further Reconsideration Order, 1 FCC Rcd. 802 (1986). These ambiguities require resolution for both closely held and widely held partnerships.

Specifically, it is unclear whether the right to remove a general partner permissibly extends to any event constituting "cause" under the partnership agreement and/or state law, or solely to the exceptionally limited instances of "malfeasance, criminal conduct or wanton or willful neglect." Id. at 803. "Cause" under the more general approach might include, e.g., financial defaults, contractual breaches, fiduciary breaches, etc. As the Commission observed, "the power to remove a general partner for cause is a right which

many limited partners reasonably perceive to be necessary to adequately protect their investment." Id. (footnote omitted). As such, they do not differ materially from lender protection provisions in traditional debt instruments which define, in objective terms, events of default permitting the lender to call the loan. The amount of "leverage" which each theoretically renders to the limited partner/lender are directly analogous as well. Moreover, the insulation requirement of a determination by an independent third party is also uncertain, since it is unclear whether a formal judicial or arbitration process is required to satisfy this requirement. Prudential therefore requests that the Commission clarify that, regardless of the number of limited partners, limited partners having the right to remove the general partner "for cause" -- as defined either in the partnership agreement or under state laws -- and where "cause" has been found by any third party independent of the limited partners -- are still entitled to insulation if all other criteria are met. These remaining provisions will serve to ensure that the limited partners remain sufficiently removed from operation and management of the media businesses, consistent with the attribution and ownership policies.

D. The Cross-Interest Policy Should Not Apply at all to Passive Investors.

An articulated goal of the attribution rules has been to provide certainty and consistency to regulated firms and their investors. As the foregoing discussion shows, however,

the operation of rules has at times failed in this objective. Modification of the attribution rules as discussed will aid substantially in this regard. In addition to modifying the attribution rules, however, the FCC must also address the corresponding aspects of the cross-interest policy. The Commission's cross-interest policy effectively removes much of the "safe harbor" potential of the Attribution rules. As such, the cross-interest policy substantially undermines the Commission's objective to establish readily ascertainable rules for media investment, and ultimately, chills such investment.

Further, the operation of cross-interest policy in the instance of "passive" investors becomes a virtual deadweight loss. Although unlikely to be viewed as problematic or threatening to any ownership policy of the FCC, cross-interest issues are theoretically raised where a "passive" investor holds a non-attributable yet substantial equity position in a television station and one of its directors also serves on the board of a co-located media enterprise. Given the origin of the cross-interest policy, as reaffirmed and clarified by the Commission in 1990, it is plain that the underlying objectives of the policy are not implicated in the instance of institutional investors. See Policy Statement, 4 FCC Rcd. 2208 (1989). The policy is designed to target "meaningful" relationships with FCC licensed entities, i.e., relationships which can result in the participation in the actual operations, most especially programming, of the station(s). In the case of

equity positions held by passive investors, the attribution thresholds should alone suffice to address "meaningful" relationships. See id. at n. 57 ("any relationship covered by the cross-interest policy that is deemed to pose a serious threat to viewpoint diversity or competition should be treated, if possible, as an attributable interest under the local ownership rules rather than subjecting it to ad hoc review as is our current practice"). Nevertheless, the Commission's 1988 proposal to modify the policy such that all equity interests would be governed exclusively by the attribution rules has never been adopted. Re-examination of the Commission's Cross-Interest Policy, 4 FCC Rcd. 2035 (1988). The pending proceeding offers an opportunity to resolve the cross-interest issues open in MM Docket 87-154 in order to reconcile the cross-interest policy, the attribution rules, and the need to facilitate investment as articulated in the Notice.

For passive investors, the application of the attribution rules, coupled with the certification required of the licensee regarding the passive nature of the investment will more than suffice to ensure that the Commission's competition and diversity goals are met. Prudential thus respectfully urges the FCC to modify the scope of the policy to provide a blanket exclusion from its coverage for any equity interests held by companies qualifying as "passive" investors under the Commission's rules.

CONCLUSION

The Commission's efforts to review its rules in order to facilitate media companies' access to capital are both timely and necessary. In addition to relaxing the attribution threshold for voting stock as proposed in the Notice, Prudential respectfully urges the FCC to adopt further specific changes, as articulated above.

Respectfully submitted,

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